REASONABLE RATES

THE principles underlying the decisions of the Interstate Commerce Commission are, for the most part, admittedly sound principles, and their number is not inordinately great. But to lawyers, and students of law, the application of these principles seems, in casual reading, to be made as whim or fancy dictates. It is a frequent complaint of the lawyer that there is no law in rate decisions.

The law is there, the principles are there, and their application has been usually made with wisdom. But there seems no clear continuity of controlling principles. There has been but a frail structure by *stare decisis* erected. Almost every question is to some extent looked upon as new.

The reason for this condition is found in the fundamental fact that the factors controlling rates are variable. Every element that enters into rate-making has a variable value. Its weight is determined by other elements. So that in no controversy can a fixed or determining value be attached to any one factor considered alone.

At first sight this gives to the rate decisions a complexion of divergence and contrariety that is puzzling and confusing. A rate is unreasonable in one instance because the length of the haul is ignored, and in another instance the mileage is unconsidered in the final determination. A preference is declared undue against one locality because of its geographical position, and in another case the natural advantages of location are equalized by similar rates to a less fortunately situated community.

The variableness of these elements complicate rate questions. But underlying the variable values, there are certain fixed principles, and if this distinction be borne in mind, it will become apparent that the rate decisions are, as a rule, in harmony, and that a system of rate law is being built up, precedents are being established, and principles fixed.

The factors entering into rates must be looked upon as a chemist conceives of atoms of strong and wide affinities. Place them in a solution of a rate controversy and they will combine with many other atoms, and the resultant molecules give the final compound its identity.

No rate factor can be considered alone. Every rate factor must be considered relatively. The effect of the factors on each other must be first determined before the final result can be announced.

This sounds more complex and more difficult than in fact it is. An examination of the elements, their variability, their effect upon each other, is not so abstruse a problem. While mathematical accuracy in rates cannot be maintained, it is easily within the realm of administrative justice to decide between reasonable and unreasonable rates, and just and unjust discrimination.

The duty of common carriers to make just and reasonable charges for services rendered in the transportation of persons and property existed at common law.[1] It is the same duty that is declared in the ACT TO REGULATE COMMERCE.

The reasonableness of charges is a mixed question of law and of fact. It raises the issue of the qualitative character of an act. To determine this issue certain evidential facts must be found and from these facts a conclusion is drawn.

The Commission's ultimate conclusion must be drawn in accordance with certain legal principles. The legal principles are few, and govern very broadly the determination of issues. Before the legal principles are applied, there may be, and usually are, certain inferences of fact. The legal principles are fixed and conclusive. The inferences of fact may change or be affected by additional facts, and are always subject to rebuttal. The two bodies of rules should be considered separately.

1. The right at common law to regulate the charges of a common carrier arose from the doctrine that when private property was devoted to a public use, the public acquired a right to the use upon reasonable terms.

In *Munn* v. *Illinois,* the Supreme Court upheld the doctrine that in property devoted to a public use, the public had such an interest that it might regulate through legislatures the charges, and consequently the revenues derived from such property by the owners. This power of regulation by the legislative authority was not subject to the review of courts. "Where property has been clothed with a public interest, the legislature may fix a limit to that which shall in law be reasonable for its use. This limit binds the courts as well as the people. If it has been improperly fixed, the legislature, not the courts must be appealed to for the change."[2]

Later decisions, while confirming the right to regulate, began to limit the legislative authority, until in *Smyth* v. *Ames,*[3] the Supreme Court declared that rates prescribed by legislative authority must yield a fair return upon the property, and when rates so prescribed

[1] Munn v. Illinois, 94 U. S. 113.
[2] Peik v. Chicago & Northwestern Ry. Co., 94 U. S. 164, 178.
[3] 169 U. S. 466.

did not yield a fair return they were confiscatory, and amounted to a deprivation of property without due process of law.

A minimum was marked to legislative authority. A line was drawn, beneath which confiscation set in. Confiscation, or deprivation of property, contrary to the constitutional right, is brought about by a revenue inadequate to constitute a fair return.

This deprivation of property may consist of two kinds: (1) The revenue derived from the rates prescribed may be less than the operating expenditures.[4] In this event the rates are unreasonably low and to attain reasonableness the rates must yield an equivalent of the expenditures.[5]

(2) The revenue derived from the rates prescribed may yield so small a margin above operating expenditures that (a) the corpus of the property is by this process being confiscated by rendering it undesirable to purchasers and therefore decreasing its value, or (b) the owners are deprived of their property right of a return upon the investment. When the sufficiency of the margin above expenditures is in question, it becomes necessary to determine what constitutes a fair return. How shall it be analyzed? No hard and fast rule can be prescribed. It is a field for discretion as broad as the field of inquiry into the reasonableness of rates.

It has been rather generally conceded that since the decision of the Supreme Court in *Smyth* v. *Ames*,[6] one absolute essential of rates is that they must yield a fair return upon the value of the property. This is not an absolute right, enforceable at the expense of all other rights and persons. In the summing up of principles laid down in that case Mr. Justice HARLAN said:[7]

"A State enactment, or regulations made under the authority of a State enactment, establishing rates for the transportation of persons or property by railroad that will not admit of the carrier earning such compensation as under all the circumstances is just to it and *to the public* would deprive such carrier of its property without due process of law."

The earlier doctrine announced in *Covington & Lexington Turnpike R. Co.* v. *Sanford*,[8] has been neglected, perhaps, but not utterly abandoned. In that case the court said:

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[4] By operating is meant all overhead expenses, etc.

[5] In this connection a question may arise as to the carrier's expenditures. They should not be reckless, extravagant, or wasteful. Chicago & G. T. Ry. Co. v. Wellman, 143 U. S. 339, 346.

[6] 169 U. S. 466.

[7] 169 U. S. at page 526.

[8] 164 U. S. 578.

"The public cannot be subjected to unreasonable rates in order simply that stockholders may earn dividends. * * * If a corporation cannot maintain such a highway and earn dividends for stockholders, it is a misfortune for it and them which the constitution does not require to be remedied by imposing unjust burdens upon the public."

The later cases following *Smyth* v. *Ames* on this question, *Northern Pacific Ry. Co.* v. *North Dakota*,[9] *Norfolk & Western Ry. Co.* v. *Conley*,[10] the *Minnesota Rate Cases*,[11] have not denied the factor value of the service to the public.

If the return upon the property were the only factor in rate-making the problem would be simple. But it must be considered in combination with that equally potent factor, the value of the service to the public. Here are two conflicting and opposing elements, constantly tending to neutralize or restrict each other. And the fairness of one depends upon the other, so that no formula can be blindly followed.

It leads us back into the original inquiry—the reasonableness of rates. A fair return may by force of circumstances be a fraction of one per cent. It is to be remembered that the legal inference that rates must yield a fair return is applicable upon rate structures as a whole. It is not a practical consideration in determining the reasonableness of isolated rates. Theoretically each rate has a cost of service and a revenue producing power, but only theoretically. Railway accounting has not progressed so far.

A whole rate structure produces a known sum, and an average cost of service, in units of ton miles, or car miles, may be estimated. But it is obvious that rates on different commodities vary above and below the average.

A single commodity may not be segregated and a rate therefore imposed that is less than the cost of service.[12] But if rates on a single commodity yield any revenue in excess of cost, no legal inference is applicable, because the margin then raises the question of a fair return.

2. That rates shall not be confiscatory is the only element in the reasonableness of rates that has a fixed legal inference.

Attempts have been made to have the Supreme Court declare other legal inferences. And while they have uniformly failed, an examina-

[9] 236 U. S. 585, 599.
[10] 236 U. S. 605.
[11] 230 U. S. 352.
[12] Northern Pacific Ry. v. North Dakota, 236 U. S. 585; and see review of former cases.

tion of those considered in the case of *Illinois Central R. R.* v. *Interstate Commerce Commission,*[13] is very enlightening upon this subject.

In that case there were presented to the court the following circumstances, which it was claimed raised the legal presumption that the rate was reasonable:

(1) A rate legally published.

(2) A rate made by competition.

(3) A rate as low as rates of other carriers on similar commodities for similar distances.

(4) A rate maintained for a series of years, and under which there has been a continuous increase in business.

(5) Rates under which a commodity moves with profit to a shipper, reduced as the market declines, increased as the market advances, the percentage of increase in the rate being less than the percentage of increase in the commodity.

(6) Rates decreased during a market depression and advanced to their former level when the depression ceases.

(7) Increases in a schedule of rates to meet increases in expenditures to care for an abnormal increase of traffic when the gross earnings of the carrier yield no greater net income.

(9 and 10) Increases in rates to pay for improvements.

(11) A rate must yield the cost of movement and contribute its fair share of operating expenses, taxes, and fixed charges.

Said the court[14] in discussing these contentions:

"A presumption is the expression of a process of reasoning and most, if not all, the rules of indirect evidence may be expressed as such. We cannot go far in the investigation of any controversy without finding ourselves compelled to infer one fact from another, but we would not therefore be justified in declaring such inferences legal maxims. It is to this that appellants invite us and seek to erect disputable inferences from conduct that may have many explanations into intendments of law. * * *

"It is conceded, as we have said, that the presumptions contended for by appellants are mixed of law and fact, except, may be, those which we shall presently consider. If either element is dominant in such presumptions, it must be that of fact. In other words, the fact must be ascertained before the law draws its inference."

The court might have gone further, and declared that not only must the fact be ascertained, but the surrounding circumstances and

[13] 206 U. S. 441.

[14] 206 U. S. 441, at pp. 459, 460.

conditions, before the law draws its inference. For if it be established, for example, that a rate was made by competition, that factor alone is not a presumption of its reasonableness. It is material and pertinent evidence, and something to which the Commission should give weight. But any presumption arising from it alone, is so faint and weak that it must have support.

And as pointed out by the court in the above cited case,[15] a legally filed rate has no presumption of reasonableness. "Of course, if a complaint should be filed before the Commission, and no proof adduced to support it, we cannot doubt but that the complaint would be dismissed; but this because of the principle that the party who asserts the affirmative in any controversy ought to prove the assertion, and that he who denies may rest in his denial until, at least, the probable truth of the matter asserted has been established."

Various elements that enter into the reasonableness of rates have from time to time been approved by the Supreme Court.[16] But the approval does not give them any force as legal presumptions, because no single element is controlling.

The Commission has the power to prescribe reasonable rates.

We are met at the outset with the difficulty of defining except in the vaguest terms what is a reasonable rate. We can only enumerate the factors entering into rate making, and, remembering that they are variable, and interdependent, state the approximate value to be attached to each.

In *Proposed Advances in Freight Rates*,[17] the Commission said: "Every question as to the reasonableness of a rate may present itself in two aspects. First, is the rate reasonable, estimated by the cost and value of the service, and as compared with other commodities; second, is it reasonable in the absolute, regarded more nearly as a tax laid upon the people who ultimately pay that rate."

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[15] 206 U. S. 441, at p. 464.

[16] Competition: United States v. Freight Ass'n., 166 U. S. 339; United States v. Joint Traffic Ass'n., 171 U. S. 505, 577; Interstate Commerce Commission v. Chicago Great Western R. R. Co., 209 U. S. 108, 119.

Value of the service to the shipper: Texas & Pac. Ry. Co. v. Interstate Commerce Commission, 162 U. S. 197.

Cost of service: Northern Pacific Ry. Co. v. North Dakota, 236 U. S. 585, and cases cited.

Value of the commodity transported: Kansas City Southern Ry. v. Carl, 227 U. S. 639, 650, 653.

Policy of the carrier in fixing rates not an element of reasonableness: Southern Pacific Co. v. Interstate Commerce Commission, 219 U. S. 433, 444.

Rates long in effect: Louisville & Nashville R. R. Co. v. Finn, 235 U. S. 601.

Local and through rates: Minnesota & St. Louis Ry. Co. v. Minnesota, 186 U. S. 257, 262; Chicago Ry. v. Tompkins, 176 U. S. 167.

[17] 9 I. C. C. 382, 401.

The cost of service and value of service are the evidential facts that determine the reasonableness of rates.

A comparison with rates on other commodities is only a method of determining the cost and value of service. The cost and value of service as a whole in the rate on the commodity compared has either been approved as reasonable or is assumed to be reasonable.

What reasonableness is in the absolute would be difficult to say. Rates may be compared to taxes for illustrative purposes but the comparison brings us little nearer a definite finding of reasonableness.

The cost of the service to the carrier for which the charge is made is a factor tending to increase rates. The value of the service to the shipper is a factor tending to decrease the rates. Each factor is made up of many elements that vary in number and in weight. And sometimes the same element enters into both factors.

Elements that enter into the cost of service may be grouped under two heads: those inherent to the commodity, and those inherent to the instrumentality of transportation. Under the first group would come weight, package, value, perishable nature, bulk, loading quality.

Under the second group would come distance, car capacity, speed, branch or main line, topography of country, direction of movement, empties, car supply, volume of traffic, direction of traffic, construction cost and maintenance.[18]

Elements that enter into the value of service to shipper are competition (rail, water and market), value, and nature of the commodity.[19]

The Commission has from time to time announced various inferences of fact that arise from certain of these elements. But, as has been noted, all of these inferences are subject to the particular circumstances and conditions of each case.

As illustrative of how the value of any one element is affected by other elements, we may examine distance. Distance is an element entering into the cost of service whose effect is apparent at a glance. But as it is obvious that rates can not be based on a mileage scale, the element of distance is used in arriving at the per ton mile earnings of the carrier from a particular rate.[20] The maxim that the rate per ton mile should decrease with the length of the haul is logical and fair. But the rate can not be measured by this unit alone. The bulk of commodities, loading capacity, etc., must be considered. So

[18] This grouping is only for convenience, and is not suggested as exhaustive either as to groups or elements.

[19] See Watkins, Shippers and Carriers, §127.

[20] This is figured by reducing the rate per 100 pounds to a rate per ton and then dividing by the distance of the haul on which it applies.

the car mile revenue is considered. The revenue per car mile[21] gives effect to the additional elements named. But the car mile revenue unit must be considered with a view to traffic conditions. If the commodity is hauled in special equipment, the return haul is empty, and commodities in usual equipment may involve a percentage of empty cars returned.[22]

So the direction of movement, the return haul of empties, must be considered. And a further unit of comparison, train mile earnings, is used, which includes the additional elements of volume and tonnage.[23]

It is evident that the facts concerning these elements, especially those relating to cost of service, would be very difficult for a shipper to adduce, and are peculiarly within the possession of the carriers. Congress has recognized this condition by enacting in the 1910 amendment to the act to regulate commerce that the carrier must prove the reasonableness of any advance in rates.

When an existing rate is assailed as unreasonable by a shipper he is forced to rely mainly upon rate comparisons. And, as has been noted, this is only a convenient form of exhibiting the result of similar cost and value of service instead of exhibiting the constituent elements, the rates used as comparisons having either been found reasonable by the Commission, or assumed so from their publication by the carriers. It is essential, of course, that the rates used for comparative purposes should be over lines and between points where the conditions and circumstances are similar. Dissimilarity of conditions means dissimilarity of the constituent elements out of which the rates are constructed, and the comparison would have no probative value.[24]

The technical nature of the evidence necessary to determine the reasonableness of rates, the inability of the shipper to adduce it, and its possession by the carrier, are responsible to some extent for the procedure before the Commission. The complainant can rarely unaided make out his case. The defendant must supply the evidential facts. And in effect, every complaint carries with it a prayer for discovery.

Decisions of the Commission and of the courts have often recited that the reasonableness of a rate is a question of fact, and that the

[21] This is derived from multiplying the average carload weight of the commodity by the rate and dividing by the distance of the haul.

[22] Western Rate Advance Case, (1915), 35 I. C. C. 497.

[23] For authorities see Watkins, Shippers and Carriers, §99.

[24] Dallas Freight Bureau v. Gulf, C. & S. F. Ry., 12 I. C. C. 223; Clark & Co. v. Buffalo & S. Ry., 18 I. C. C. 380; Parfrey v. C. M. & P. Ry. Co., 20 I. C. C. 103; Watkins, Shippers and Carriers, §110, and citations.

finding of the Commission thereon is final. And as the process of determining the evidential facts, and drawing therefrom their proper inference and legal conclusions, is often obscure, it sometimes seems that rate decisions are mysteriously effected. It may appear that the Commission thrusts its hand into the darkness, and a reasonable rate is plucked back like a rabbit from a conjuror's hat.

There is, of course, no step taken towards the ultimate finding which is not logical.

The process of determining the reasonableness of rates consists of two stages. The first stage, finding the evidential facts, is within the exclusive discretionary power of the Commission and its findings so far are final. The second stage is deductive reasoning, and presents a question of law. It is a question of law, for example, when the Commission determines the reasonableness of rates upon the conclusion that rates equitable to shippers are therefore reasonable.[25] Here the evidential facts did not warrant the conclusion of reasonableness.

When the evidence is a "mass of facts—out of which experts could have named a rate," the Commission's conclusion from those facts, is a conclusion of law. The findings of fact being final, the legal conclusion therefrom was proper.[26]

The conclusion of reasonableness must always be supported by evidential facts. When the facts conflict, or their relative weight is in question, the Commission's finding is final. And in this field there are wide limits to the flexibility of its judgment. But it is not a tribunal of arbitrary nor unlimited powers.

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[25] Southern Pacific Co. v. Interstate Commerce Commission, 219 U. S. 433, 444.
[26] Interstate Commerce Commission v. Union Pacific R. R., 222 U. S. 541, 550.